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THE ITALIAN BANKING CRISIS.

ANY one who is at all acquainted with the history of banks of issue in the principal countries of the world knows what violent crises have been brought about by the vicious policies and methods of administration adopted by governments and banks in regard to credit. Political economy is able plainly to indicate true scientific principles deduced from observation, to cite instances of the harm which has followed when these principles have been forgotten, even to foretell the disastrous consequences which must follow whenever an attempt is made to settle matters relating to banks of issue without regard to economic laws; but all this is not enough. Harsh experience alone can make a people understand the errors which they have committed and lead them to accept counsel of men of science. We have seen and felt all this in Italy during the last few years. It will surely be useful for other countries to know the details of the panic through which the Italian banks have passed; for this experience has shown how well founded are certain conclusions of economic science. It has shown also to what inevitable results government interference, politics, and other like influences lead in matters which ought to be regulated solely by the principles of economic science and practice. It will appear on reviewing briefly the history of the Italian banks of issue, that they have committed grave errors in practice, Government and Parliament heedlessly consenting or inciting thereto, and that these errors have been

accompanied, happily in but one bank (the Banca Romana), by frauds, corruption, and a squandering of money. This has resulted in such a condition of affairs that we have been obliged to enact, at any cost, a new law for the regulation of banks of issue and put a stop to the disorder, or in colloquial phrase, to the "anarchy", of our bank-note circulation. In the long record of commercial crises there have certainly occurred periods analogous to that through which Italy is now passing; but if the present situation in Italy is in certain respects similar to the situation in England prior to the passage of the *Bank Charter Act* of 1844, especially as regards over-issues, the Italian banking crisis differs, at least in some special features, from other crises. One peculiarity among others is that the banks of issue, whose fate has been constantly in doubt during the last ten years, are subject to the caprices of government control; that is to say, to the caprices of the ministers who may have the direction of public affairs and who have forgotten the first principles of scientific banking. It happens, too, that the banks have ignored the prudent rule so neatly expressed by the Count de Mollien in the words, "*pour ne jamais finir, une Banque doit être toujours prête à finir.*"¹ Through operations incompatible with the functions of banks of issue, the Italian banks have got themselves into a condition where it is impossible for them to keep the circulation of their notes within the limits fixed by law, and redeem notes at sight without restriction. What with one bank, a Roman one, that has lost all its capital twice over, and other banks that in point of fact do not redeem their notes at par; with a metallic currency at a premium of from eleven to twelve per cent., and an absolute dearth of subsidiary coin, one may well speak without exaggeration of a banking crisis.

But it is time to pass to an account of the details which have characterized the crisis, that we may be able afterward to seek out causes and effects and indicate the measures which have been taken to mend affairs.

¹ "In order never to close, a bank should always be prepared to close."

I.

From 1876 to the present time Italy has had six banks of issue, of different financial strength. The Banca Nazionale nel Regno d'Italia (National Bank in the Kingdom of Italy) with a capital of 150,000,000 lire (\$30,000,000), the Banca Nazionale Toscana (National Bank of Tuscany) with 21,000,000 lire (\$4,500,000), the Banca Romana (Bank of Rome) with 15,000,000 lire (\$3,000,000), the Banca Toscana di Credito (the Tuscan Bank of Credit) with 5,000,000 lire (\$1,000,000),—these four banks are joint-stock corporations with regular shareholders. The Banca di Napoli with 68,750,000 lire (\$9,700,000), and the Banca di Sicilia with 12,000,000 lire (\$2,600,000), have no shareholders, both being public institutions: their holdings are not private property, and in case of liquidation it would be carried out by the State. Neither of these two banks, therefore, is called upon to declare dividends: of net earnings, part goes to augment the capital, and part is devoted to philanthropic objects.

The six banks of issue above named have been governed by the law of April 30, 1874, which accorded them the privilege of issuing notes to the amount of three times their capital, provided they kept a reserve in coin or legal tender notes, equal to one-third the amount of their own notes in circulation. The capital was fixed by the government for each bank at amounts already indicated in the figures above quoted. The chief purpose of the law of 1874 was to fix a limit to the amount of notes issued by the banks and by the State; for since May 1, 1866, Italy had been under a régime of legal tender paper money (*cours forcé*), and notes had been issued on government account aggregating 860,000,000 lire (\$172,000,000). The law of 1874 aimed also to reduce the banks to some uniformity of practice. These banks had had no common basis of operation. So that a note of the Banca Nazionale nel Regno d'Italia was not convertible at sight into coin, while the two state banks no longer issued regular bank notes but only certificates of deposit (*fedi e polizze*). The law of 1874 also aimed to extend the circulation

of the bank notes by taking away their provincial character. It was thought, moreover, that the six banks of issue might be combined into a union (*consorzio*) or association for the purpose of loaning to the government a sum not exceeding one milliard of lire (\$200,000,000) in legal tender notes, which would thus constitute a national debt. At the same time the law authorized the banks to issue on their own account a total of 755,250,000 lire (\$151,050,000). These notes were a legal tender, but were redeemable on demand in coin or in the notes of the associated banks, that is to say, the legal tender notes issued on government account.

It is to be remarked that the law of 1874 satisfied neither the advocates of the principle of a plurality of banks of issue (as that principle is applied in the United States) nor those who preferred a single bank of issue modeled upon the Bank of France. In fact, on the one hand, the number of institutions of credit having power to issue notes was strictly limited, while, on the other hand, the law tended to hold the banks in a condition of equality—to give to each full scope and freedom of expansion. The law regarded a certain degree of emulation and competition between the six banks as useful and beneficial. It was hoped that in this way commerce and industry might receive some advantage, and that the power of the chief bank, Banca Nazionale nel Regno d'Italia, might be held in check by the five other institutions. But the authors of the law of 1874 intended it to be essentially a measure for regulating the circulation of paper currency, and they hoped to put an end thereby to the disorder which had been brought about through the free issue of notes by popular and commercial institutions of credit, by savings banks, and even by private individuals. They did not attempt to decide the relative merits of single and of associated banks of issue—no one had that matter in mind; but later, after the abolition of forced circulation and the resumption of specie payments, the one or the other system should have been chosen: this was the idea of the authors of the law of 1874. From 1874 down to the discontinuance of forced circulation and the resumption

of specie payments (April 12, 1883), the development of the Italian banks was normal. I give the most important figures for the period 1873-1882, in millions of lire :

YEAR.	Capital and Reserve December 31.	Notes in Circulation, and other Debts payable at sight December 31.	Bills and Loans December 31.	Total Discounts and Loans made during the year.	Commercial Bills not paid December 31.
1873	303.3	790.4	539.2	2398.0	6.6
1874	311.4	761.4	470.2	2169.7	7.5
1875	325.9	729.9	427.3	2077.1	10.7
1876	330.3	759.2	421.2	1801.2	16.1
1877	334.3	765.3	453.6	1824.8	19.7
1878	340.8	815.8	477.6	1730.7	20.5
1879	344.5	853.1	511.3	2116.6	19.3
1880	348.5	911.8	570.8	2402.0	17.1
1881	352.3	861.7	517.6	2543.4	16.4
1882	357.6	872.1	523.5	2599.0	17.3

Many observations might be made upon these figures, but as we must hasten on to the last period, 1883-1892, we shall content ourselves with noting that in 1873 the amount of loans and discounts was very high, corresponding to the general expansion of business which preceded the crisis of that year; in 1874 a period of contraction began, and not till 1879 did business tend to become more active. But the commercial bills unpaid [*effets de commerce en souffrance*] as early as 1876 amounted to a considerable sum, and from that time on they maintained themselves at a figure which would scarcely be found on the books of banks of issue in other countries. It is, indeed, an indication of how little restraint was used in the operations of some of the banks, and suggests that a reasonable amount of prudence would have counseled proceeding with much greater caution in the new era opened by the abolition of the forced circulation.

The law of April 1, 1881, provided for a return to specie payments; two years later, April 12, 1883, the doors of the treasury opened for the redemption of national notes issued on account of the government by the associated banks. A loan of 640,000,000 lire (\$128,000,000) and the issue of 340,000,000 lire (\$68,000,000) in national notes (in denominations of one and two dollars) made it possible to retire the legal tender notes

in forced circulation. This operation sensibly modified the composition of the currency, and made necessary a reorganization of the banks in order to give greater elasticity to their circulation, and to render possible and effective the change from their notes to coin. Bills had been presented to Parliament before 1883, but opportunity to discuss them had been wanting, and we found ourselves about to resume payment without having done anything to better the situation of the banks of issue, which had, indeed, during the period of paper currency, reaped a considerable net profit. The bill presented by MM. Magliani and Berti, on November 26, 1883, initiated the long succession of bills dealing with banks of issue, which have brought us through many sad vicissitudes to the new law of August 10, 1893 ; to this law we shall devote our attention later. The parliamentary machine is pretty slow. Ten years, a crisis, and a number of scandals, have been necessary to bring about a law which every one has for a long time recognized to be altogether indispensable to the interests of the country and of the treasury.

After the change to a metallic basis, Italy experienced, down to 1887, a period of excessive speculation. On April 12, 1883, the premium on gold was reduced to zero. The demand for the redemption of notes was at first considerably less than had been prepared for. The public felt absolute confidence in the notes and preferred them to coin. Italian five per cent. rentes, and nearly all Italian securities, experienced a considerable rise. Banks of issue, contrary to their previous intentions, continued to discount at five per cent., and bills of exchange found a ready market in foreign countries, especially in France and Switzerland. At the same time good interest bearing bonds and other securities were sent abroad, creating thus, temporarily, a large credit in favor of Italy. Italy was enabled to make payment for the coin reserves accumulated for the resumption of specie payments, and to pay the balance of international trade, at that time unfavorable. In the five years 1884-1888, the merchandise imported into Italy exceeded the exports by more than two milliards of lire ; the excess amounted in 1887 to 603,-

000,000 lire. In 1884, however, confidence in the Italian monetary regime was such that institutions of credit and foreign bankers eagerly accepted Italian paper, and this placed at our disposal large resources which we abused. The rate of discount fell from five to four per cent. and even to three and one-half per cent.; foreign exchanges were favorable to Italy.

This lasted but a short time. As early as 1884, in the beginning of the autumn, owing to the outbreak of cholera, the bad harvests, and other secondary causes, the conditions of the money market underwent their first depression. But the real crisis in monetary affairs and in public credit came upon us in April, 1885; Italian securities fell in Paris and London, the exchanges rose, gold and silver left the country. In April, 1885, according to the figures of the custom house (which are notoriously incomplete), the exportation of gold and silver was 85,000,000 lire, and the importation 16,000,000; excess of exports 69,000,000. In the same month the cash reserve of the Treasury shrunk 59,000,000, and that of the Banca Nazionale, 26,000,000 lire. The payment of the notes grew more difficult, and the banks of issue interposed to float Italian securities abroad and depress the exchanges. The rate of discount was raised to six per cent., but this and other similar measures could not permanently ward off the crisis. The depression returned in 1887, to continue down to the present time, when we have had an exacerbation of distress, as we shall presently see.

One cause of the crisis of 1887 is found in the extensive building operations carried on and encouraged by a system of loans granted by loan associations to builders, often upon very easy terms. Another cause is found in the diminution of free capital. Foreigners had withdrawn their contributions; they refused to discount Italian commercial paper, or to extend the time on their securities, or to engage in new commercial and industrial enterprises. The withdrawal of foreign capital was a very severe blow. Italy had need then, as she has now, of foreign capital in her industry and commerce; but the withdrawal was an inevitable consequence of the reappearance of a premium

upon gold ; a premium which by its frequent oscillations deprived credit operations of all security and stability. Every resource should have been strained to do away with the premium ; but the banks of issue which should have coöperated with the treasury to compass that end did not find themselves in a condition to act effectively, and by their shortcomings they aggravated the evil.

The fundamental error committed by the banks of issue since 1885 has been the undue exercise of their functions as note issuers, and the employment of their notes in operations not compatible with the nature and purpose of a bank issue ; that is to say, in granting long credit, and that based not upon commercial paper but on real or industrial and agricultural securities. The law of 1874 fixed the issues of the banks at 755,250,000 lire ; but, although this limit was never passed before the resumption of specie payments, after 1887 issues of notes were made aggregating a much larger sum. I think it will be of use to present the figures relating to the circulation of notes of the banks and of the government since 1871 :

MILLIONS OF LIRE.

YEAR.	Notes issued on account of the State.	Notes of the six banks of issue.	Total paper in circulation.	Total cash re- serve of the six banks. ¹
1871	629.0	577.5	1206.5	307.4
1872	760.0	623.3	1363.3	282.1
1873	790.0	664.3	1454.3	306.5
1874	880.0	633.2	1513.2	318.4
1875	960.0	621.2	1561.2	276.1
1876	960.0	646.0	1586.0	300.1
1877	960.0	628.5	1568.5	278.2
1878	960.0	672.2	1612.2	318.9
1879	960.0	732.4	1672.4	322.9
1880	960.0	768.9	1688.9	323.2
1881	960.0	735.5	1675.5	296.7
1882	960.0	732.3	1672.3	303.5
1883	718.0	793.9	1511.9	449.6
1884	610.8	899.0	1509.8	496.3
1885	493.2	948.4	1441.6	433.6
1886	446.6	1031.8	1478.4	451.5
1887	395.1	1075.7	1470.8	451.2
1888	346.3	1074.8	1421.1	460.4
1889	344.1	1114.1	1458.2	438.7
1890	342.8	1126.4	1469.2	409.6
1891	341.9	1121.6	1463.5	442.7
1892	341.4	1138.3	1479.7	447.0
1893	332.9	1157.1	1490.0	445.9

¹ Metallic reserve.

An unauthorized or illegal issue of several hundred millions of lire was tolerated by the government at the end of 1885, and, as if that were not enough, the circulation was increased in 1889 for carrying out transactions which had nothing to do with the banks of issue. In order to aid some loan associations seriously involved in operations connected with the building of houses at Rome and elsewhere, the government, in 1889, allowed the Banca Nazionale to increase its issue by 50,000,000 lire. The disorder reached such a point that there were in circulation four kinds of notes: (1) those issued in conformity with the law of April 30, 1874, to an amount equal to three times the capital stock and coin reserves of the banks ("productive" issue); (2) notes guaranteed by an amount of coin reserve equal to the amount of notes issued ("unproductive" issue); (3) notes not guaranteed by any coin reserve ("abusive" issue); and (4) notes constituting loans made on the authority of the government ("incalculable" issue).

There is no need of dwelling upon the deplorable consequences of these excessive and unrestrained issues. The banks enlarged their discounts and loans, but the amount of unpaid bills increased in the same ratio, and the redemption of notes became still more fictitious and illusory. The amount of "immobilized" capital, that is, of resources *not* convertible into money on short notice, became considerable; the amount of true commercial credit granted, that is to say, the amount of genuine commercial bills discounted as compared with loans made upon landed and proprietary security and accommodation loans, grew daily less. The state of affairs was made sufficiently known by an inquiry undertaken by the government after the revelations touching the situation of the Banca Romana. This was done by some members of the House of Deputies, who made use of a report presented to Minister Miceli by Senator Alvisi in 1889, after an inspection of the Bank. The inspection made in January, 1893, under the direction of Senator Finali, now president of the Corte dei Conti (Bureau of Accounts), resulted in a voluminous report, by the aid of which we shall attempt to show

the critical situation of the banks of issue in the beginning of 1893.

The commission had authority: to examine the figures showing the amount of resources made unavailable for immediate use ("immobilized") and the *emplois directs* to which capital is put (being but another way of immobilizing capital); to ascertain the amount of bills unpaid and to be extended; the make-up of the commercial paper of each bank; the losses suffered by each, etc. The more significant figures are collected in the subjoined table, in millions of lire (January 10, 1893):

	Banca Nazionale nel Regno d'Italia.	Banca di Napoli.	Banca Nazionale Toscana.	Banca Romana.	Banca di Sicilia.	Banca Toscana di Credito.
Capital and reserves (surplus fund)	190.0	71.5	23.4	20.0	23.1	5.5
Capital immobilized	142.0	27.7	6.7	18.2	3.0	1.3
<i>Emplois directs</i>	98.0	49.4	8.3	1.6	7.1	7.7
Bills unpaid and renewed	49.4	49.3	4.6	16.0	13.9	
Estimated losses	17.0	39.5	4.5	20.0	7.7	
Circulation	575.2	273.4	101.8	137.0	65.4	17.1
Coin reserve	230.1	103.4	44.6	24.8	36.7	6.1
Discounts	363.9	97.5	60.9	61.0	31.8	2.4
Advances	63.8	28.2	4.6	1.5	8.8	2.0

It appears from these figures, which are official, that the banks with exception of the Banca Toscana di Credito, the smallest of the six, have made unavailable for present use a great portion of their assets and have lost much of their capital. I have said that these figures are official; if reference is made to the data furnished in the particular reports for each bank the results arrived at are still more disheartening. It appears that the funds which are not available amount for the Banca Nazionale nel Regno to 320,700,000 lire, of which 137,900,000 is "bills renewed"; for the Banca di Napoli to 161,000,000; for the Banca Nazionale Toscana to 18,000,000; for the Banca Romana to 100,200,000; for the Banca di Sicilia to 26,500,000; for the Banca Toscana di Credito to 1,800,000 lire.

It would be unjust, however, to hold the banks responsible for all this immobilization of resources; in a great measure the

immobilization is the result of government intervention and politics in the administration and direction of these six institutions of credit. The government, for example, is responsible for the loans made to the Bank of Turin, the subsidy granted to the Province of Cagliari, the immobilization of the notes of the Banca Romana in the vaults of the Banca Nazionale, etc. But it is none the less beyond question that the Italian banks have absolutely lost sight of the purpose and proper functions of banks of issue. To be convinced of this we need only note that three of the banks have extended credit upon landed property (*credit foncier*); one, the Banca di Sicilia, has made loans upon agricultural paper; and all six have discounted the bills of farmers, proprietors, manufacturers, professional men, contractors—in a word, of such as need long credit, certainly longer than three months. With a budget of bills of this nature in its safes, with the immobilization of its immediate capital by *emplois directs* (that is to say, investments in the form of bonds or securities guaranteed by the State, exchequer bills) with bills unpaid or extended, it is not difficult to understand that the notes of the banks could not be effectively redeemable at sight, and that sooner or later they must fall in value as compared with coin. At present the depreciation of bank notes fluctuates between eleven and twelve per cent.

The investigation in January of this year disclosed chiefly the deplorable condition of the Banca Romana. Indeed it was known already that there had been irregularities in the past, but no one had looked for the revelations of the inquiry. The report presented on March 15, 1875, to the chamber of deputies complained of grave irregularities on the part of the management of the Banca Romana. It had bought up some of its own shares and the report goes on to say, "what is worse, its capital no longer exists except in appearance, for there is a deficit much in excess of its capital." Since the foundation of the bank, large amounts of its securities had gone to protest, and instead of charging the shrinkage to the account of losses, this paper appeared on the balance sheet at its face value; so

that when it was found desirable to change the system, after 1870, it became necessary to reduce the value of a great number of the assets by 50, 75, or even 99 per cent. But government officials are possessed of a truly remarkable optimism and an abiding faith in the ability of the bank to make good the losses of the past.

We read in the report presented to the Chamber of Deputies, February 21, 1879, by the Ministers Majorana and Magliani: "The difficulties in which some of the smaller banks are struggling may lead to real disasters if a remedy is not soon applied." In spite of this, ten years passed without any one taking any thought whatever as to the remedy. Finally, in 1889, the situation had become intolerable; the Banca Romana was less and less able to redeem its notes; the government determined to act; it ordered an extraordinary inspection, but it kept the result from the public. Senator Alvisi, however, found means to inform the Senate, June 30, 1891, of a part of the irregularities of the Banca Romana discovered by him; for example, that it had an unauthorized, secret, and illegal circulation to an amount of more than 25,000,000 lire; that for five years past accounts had not been balanced; that the books showed the absence of 4,000,000 lire of collaterals. But they imposed silence on him in the name of the country's credit, and through fear of injuring the country he kept still. So the Banca Romana continued in its illegal issues, all the more since it was released in August, 1891, from the obligation of redeeming its bills held by other banks.¹ Once relieved from the *riscontrata*, and the curb of the redemption of its notes in coin from the public, the Banca Romana was enabled to increase its issues to such an extent that the inquiry found, on January 10 of the present year, that it had in circulation 137,000,000 lire, of which 64,500,000 were illegal; that is to say, it had nearly double the issue that the law of June 30, 1891, allowed it (70,000,000 lire). The same inquiry

¹ This obligation is known in Italy as the *riscontrata*. Each bank is required, at stated periods, to redeem such of its notes as are held by other banks, by exchanging for them notes of the banks by which they are held, or by redeeming them in coin.

revealed a deficit in the bank's accounts, concealed by fictitious entries, of 28,500,000 lire.

I do not dwell on the other facts discovered by the inspectors, for it would be necessary to refer to and explain many matters not of first-rate importance, or to make excursions into what is not properly the economic field, but rather political and moral. We come then to certain general considerations relating to the causes and the effects of the Italian banking crisis.

II.

The causes of the crisis of the Italian banks might be summed up in the sentence: the Italian banks of issue have followed a course directly contrary to that which the issue of notes requires, that is to say, they have created debts payable at sight immediately and without recourse. But this judgment is too categorical and will scarcely give a precise idea of the crisis and its origin. In every case it is easily seen why and how the banks have misconceived the principles which ought to govern their conduct. Until the abolition of the forced circulation the banks of issue lived in Italy, as elsewhere where errors have been made in regard to the forced circulation, in an artificial atmosphere. For seventeen years (from May 1, 1866, to April 12, 1883) they had no occasion to know the difficulties inherent in the payment of their notes in coin; for the notes were legal tender, and if they were presented for redemption the banks could always redeem them in the notes of the associated banks (see page 4) which amounted to about 940,000,000 lire, and which were still preferred to the notes of the banks themselves (about 750,000,000). But with the resumption of specie payments they found themselves under new conditions, all the dangers of which they had not appreciated. And whereas they should have used extreme prudence in regard to issues and in their discount business, they had allowed themselves to be drawn into excesses and mismanagement in the one or the other branch.

The resumption of specie payments was followed by a period of great speculative activity. A proof of this fact is found in

the annual increase of discounts and loans by the banks. I have already indicated the movement of these operations up to 1882 (page 5) ; it is interesting to watch it also for the years following, and that not only for the banks of issue, but also for the other institutions of credit.

ANNUAL AMOUNT OF DISCOUNTS AND LOANS (MILLIONS OF LIRE).

	BANKS OF ISSUE.		ORDINARY CREDIT ASSOCIATIONS.	PEOPLE'S BANKS AND COÖPERATIVE CREDIT ASSOCIATIONS.	BANKS OF AGRICULTURAL CREDIT.	AMOUNT OF DEPOSITS RECEIVED BY ALL CONCERNS WHICH RECEIVED SAVINGS.
	Amount of loans and discounts.	Bills unpaid Dec. 31.				
1881	2543.4	16.4	2031.5	594.9	158.9	979.3
1882	2599.0	17.3	2347.0	692.1	172.8	1040.8
1883	2519.8	16.5	2664.3	746.1	141.7	1151.0
1884	2548.2	15.4	2670.2	825.7	116.9	1302.8
1885	3639.3	14.4	3037.1	1002.1	167.5	1420.2
1886	4438.0	16.8	3501.4	1245.7	174.4	1632.3
1887	5181.4	22.9	4459.7	1432.7	180.5	1692.4
1888	4736.2	31.5	4354.6	1417.8	193.2	1763.3
1889	4671.2	38.4	— [†]	— [†]	— [†]	1789.4
1890	4344.2	41.1	—	—	—	—
1891	3993.0	42.2	—	—	—	—
1892	3640.5	46.2	—	—	—	—

It is very interesting to compare the years 1885–1887 with the four years preceding, and note the considerable increase of business; the banks of issue in 1887 discounting bills and placing loans for 2,548,000,000 lire, and three years after for a sum twice as great, 5,181,000,000. The same holds true, in a slightly less degree, for the other institutions of credit. Americans are accustomed to considerable fluctuations in their statistical figures and will perhaps not be surprised at the facts I have pointed out. But we must bear in mind that the economic movement of Italy is very slow, that its agricultural and industrial production, its international commerce, all the manifestations of its economic activity are feeble and develop slowly. Now this abnormal development of the business of the banks of issue has been the principal cause of the difficulties into which they have fallen, and it has resulted in the country's being at

[†] For the last four years the figures are still wanting.

present without metallic money and burdened with national notes and bank notes inconvertible, not in law, but in fact.

A bank of issue, as everybody knows, ought to discount commercial paper, representing actual transactions, and of short date—not exceeding three months. The Italian banks discounted paper for persons who wanted a long term of credit, and even paper not representing commercial transactions (accommodation bills); they lowered the rate of discount even in the time of the crises in 1885, 1887, 1889 and later, and if they raised the rate it was done late and insufficiently. Speculation suffered no penalty, and spread into all fields. In building enterprises, on the stock exchange, in trade the official rate of discount never exceeded six per cent., when it should, perhaps, have risen to ten or twelve per cent.; and this state of affairs is readily comprehensible. The banks of issue had always available means, for they no longer recognized any limit to their issues, and had no fear of a run on the bank for the redemption of the notes, because they could without difficulty increase the circulation. But the question may occur, was there no danger of a run? The answer is very simple; the Government, not wishing the banks to lose their metallic stock, permitted them by all possible expedients to render the redemption fictitious and ineffectual, and when recourse was had to the courts of justice, they declared in substance that the question belonged to the province of the Government. The public, seeing that the attempt to force the redemption of the notes was useless, gave up the effort, and we then witnessed the interesting spectacle of a people who, taking the law for right, did not demand the redemption of the bank notes, but submitted to the payment of a brokerage of eleven to twelve per cent. in order to get coin.

Banks of issue ought to have their assets realizable as promptly as possible, in order to meet their engagements, which are for the most part on short time (notes and deposits on call). The banks of issue of Italy forgot this elementary truth and used their notes in mortgage loans, for a permanent advance of 68,000,000 lire to the Treasury (which has a large floating debt with no possibility

of redeeming it); in discounting bills which were not paid at maturity, or paid only in part, and which the banks were obliged, willing or unwilling, to renew; and in other operations of a like nature. The issue being covered only in part by the reserve and by good commercial paper, the notes necessarily depreciated, and this depreciation was increased by the fact that the true situation of the bank was known.

But it would be a useless task, after what I have said, to confront the Italian banks of issue with economic principles by which banks of issue are to be guided—principles which are the most certain and undisputed of any in economic science. I may rather resume the consideration of the general and special causes which determined the Italian banking crisis, in order to bring these remarks to a close. Among the general causes we ought certainly to include the embarrassment arising from the financial condition of the State, the communes and the provinces; of the State especially, whose budget, since 1885, has presented a deficit which threatens to become chronic. The growing difficulties of the Treasury, which has a considerable floating debt and has to make large payments in gold every year to foreign creditors; the increase of the State debt; the general economic depression in consequence of bad harvests, the political protective tariff, and the immobilization of capital; the crisis in building operations, particularly in Rome, where so many fortunes have been lost during the last few years,—all these things, with others of the same nature, have had a disastrous influence on the conditions under which the banks of issue have had to work. In short, without entering into details which would show us the economic and financial condition of the country, it is sufficient to note that the Treasury is required to pay annually to foreign creditors nearly 250,000,000 lire, to be convinced that the stable and favorable monetary conditions in which the country might be able to save its stock of money, and in which the banks could easily pay and receive coin, are wanting. Now, Italy, which has no gold or silver mines and does not hold foreign bonds or values, always holds a slight stock of specie; and further she is not a

creditor but a debtor in international commerce. Thus, we are never in a stable monetary condition; a fact which has prevented the formation of a current of metallic money, ebbing and flowing between the banks of issue and the country.

But in reference to the banking crisis it is the special causes with which we are particularly concerned here. They may be summarized as follows: The immobilization of a great part of the assets of the banks in operations alien to the functions of banks of issue; the bad character of a part of their business, as shown by the unpaid bills and the extension of loans; the inadequacy of their metallic reserves; the illegal issues of notes, excessive and without security; and finally, the mismanagement in the granting of credit. We have already explained what were the various causes at work, and it is unnecessary to insist on them.

In regard to the assets, the figures of the losses sustained by the banks, the necessity of winding up one of them—the Banca Romana—as well as the rise of foreign exchange, the depreciation of the bank notes, the premium on gold, the exodus of metallic money, the decline of Italian bonds and securities, reveal the disastrous consequences of the errors committed during the last few years. Some of the figures need full discussion. The Italian rentes [5% (4.34% net)], which were quoted at Paris during the second half of 1886 as high as 101.25, and had fallen in 1889 to 91.72, were still as high as 91.42 August 16, 1892; but a year after that date, August 16, 1893, they stood at 86.25, and on the 16th of October, 1893, they were quoted at about 83.50. The movement of the exchanges between Rome and Paris is still more instructive, in that it reveals all the difficulties of the monetary situation:

	1881	1882	1883	1884	1885	1886	1887	1888	1889	1890	1891	1892
MEAN OF THE YEAR.	101.46	102.30	99.92	99.97	100.37	100.21	101.81	100.96	100.66	101.06	101.47	103.75

August 16, 1892, it stood at 103.90; a year later, August 16, 1893, at 100.40; and at present it oscillates about 112.00. Now, the gold point for Paris may be counted at about 100.40; there

is therefore a premium on gold of more than eleven per cent., that is to say, we have relapsed into a worse condition than in the years of forced circulation. Is it necessary, after this, to insist on the effects of the banking crisis, on the burden which it imposes on the government in the payments which it has to make to other countries, and also on industry and commerce, on consumers, in their purchases and in their payments abroad, or to recite the embarrassments we suffer from the exodus of all coin, even including fractional currency? I believe not. And therefore I proceed directly to the consideration of the new law of August 10, 1893, dealing with banks of issue, by which it is believed we shall be able to put a stop to the crisis, by reorganizing the banks and imposing new restrictions upon them.

III.

A succession of scandals which cannot be enumerated here have been necessary in order to induce Parliament to find the time and the energy to discuss and pass a new law. For ten years every effort in this direction has failed. But the urgent necessity of providing for the liquidation of the Banca Romana, together with the necessity of finding some means of obliging other banks to reduce their real investments and their note issues, has finally compelled Parliament to turn its attention to the reorganization of the banks. The law of August 10, 1893, officially recognizes the disappearance of the Banca Romana, and the consolidation of three other banks, viz., the Banca Nazionale nel Regno, the Banca Nazionale Toscana, and the Banca Toscana di Credito, into a new bank, the Banca d' Italia. In this way d' the number has been reduced from six to three, the Banca Italia, and the two banks of Naples and of Sicily. These last retain their capitalization at their earlier figures, while the Banca d' Italia will possess a nominal capital of 300,000,000 lire, divided into 300,000 shares of one thousand lire each. But the paid-up capital of the Banca d' Italia will amount to only 210,000,000, and since the three banks which unite to form the Banca d' Italia already possessed a paid-up

capital of 176,000,000, the paid-up capital would have to be increased by only 34,000,000 lire ($210 - 176 = 34$) during the six months following the promulgation of the new law. The right to issue notes is granted to the Banca d' Italia and confirmed to the banks of Naples and of Sicily for a period of twenty years, counting from the date of the promulgation of the law. The maximum limit of circulation for these banks of issue is fixed for a period of four years at 1,097,000,000 lire apportioned as follows: The Banca d' Italia 800,000,000, the Banca di Napoli 242,000,000, the Banca di Sicilia 55,000,000. When these four years are past, each of the banks is to begin a biennial reduction of its circulation, by an amount so proportioned, that at the expiration of fourteen years after the law goes into effect the circulation will be reduced in the case of the Banca d' Italia to 630,000,000, in that of the Banca di Napoli to 190,000,000, and in that of the Banca di Sicilia to 44,000,000, a total of 864,000,000 lire. If at the end of fourteen years any bank is not possessed of a capital or of assets amounting to one-third of its notes, it is required before the expiration of three months to reduce its circulation to that proportion. The reduction which the circulation of one of the banks suffers in this way will inure to the benefit of the other banks, which may possess or pay up the proportionate amount of capital necessary to secure the additional circulation which thereby falls to their share. Before the expiration of the fourteenth year a commission is to be appointed, consisting of seven members, two being elected by the Senate, two by the Chamber, and three appointed by the Crown (that is to say, by the Government), whose duty it shall be to appraise the capital or assets of the banks of issue for the purposes contemplated by the law.

The circulation of any one of the banks may exceed the limit prescribed by the law so far as their notes are completely covered by legally recognized metallic money, or by gold bullion actually held in their vaults. Notes representing ordinary and extraordinary advances by the banks to the state, are not to be considered as comprised within the limits of circulation fixed by the law.

The reserves of the banks of issue are to be increased within a year to forty per cent. of their circulation (they are now estimated at thirty-three per cent.). It is to be made up of coin legally current in Italy, foreign coin accepted as legally current within the Kingdom, or gold bullion, to the extent of thirty-three per cent.; and the remainder (seven per cent.) may be made up of bills of exchange on foreign countries bearing first-class signatures which are recognized as such by the Minister of the Treasury.

In the preparation of the notes, the State and each one of the three banks of issue will be associated in such a manner that neither the State nor any one of the three banks will be able separately to turn out a note in its completed form. The conditions under which notes are to be printed will be defined by royal decree. Likewise with respect to the manner of replacing them when soiled or thrown out of use, as well as the provisions for canceling and destroying them. A decision will be reached at the same time as to the amount of notes to be supplied to each bank, and the means of control to be employed for ascertaining the use to which the notes are put. The Government will decide upon the form, the size, and the design of the notes to be printed. The expense of printing the notes is defrayed by the banks, the printing and supplying of the notes leaving no responsibility resting on the State either in relation to the public or in relation to the banks.

Holders of the notes have the right to demand of each of the banks the payment at sight to the bearer of such notes as it has issued,—payment to be made in coin legally current in the Kingdom, at the cities of Rome, Bari, Bologna, Catana, Florence, Genoa, Leghorn, Messina, Milan, Naples, Palermo, Turin, Venice, and Verona. During the first five years after the law goes into effect, the notes of the Banca d' Italia, as also those of the Banca di Napoli and of the Banca di Sicilia, are to be a legal tender in the Provinces where the concern which has issued the notes in question may have a main or branch office or an agency, with the obligation to redeem the notes in coin. So long as the notes

retain their legal tender character, the rate of discount is to be the same for all the banks concerned, and must not vary without the authority of Government. They may, however, discount at one per cent. less (than the ordinary rate) the papers of the country banks, of banks of discount, and of those which do business in agricultural credit, and which are organized: (1) to act as intermediaries between petty commerce and the banks of issue; (2) for the discount of the warrants of the general warehouses and entrepôts. This special discount must, in the case of the Banca d' Italia, not exceed 70,000,000; in that of the Banca di Napoli, 21,000,000; and in that of the Banca di Sicilia, 4,500,000 lire.

All the banks are required to receive the notes of other banks wherever these latter have a main office, a branch establishment, or an agency. As long as the legal tender character of these notes continues the conditions of their redemption between the different banks¹ is fixed by a royal decree, which ought, during the present year (1893) to be presented to Parliament to be enacted as a law.

The bankers are to pay a tax of one per cent. upon the actual average of their circulation, deduction being made of the sum total of the reserve prescribed by law. Over and above this normal tax, the banks pay to the State a special tax—amounting to double the rate of discount—for the excess of their circulation above the limits fixed by law, or in excess of the prescribed proportion to their metallic reserve.

A special reserve, equal at least to 40 per cent. of the note issue, is required as a security for the debts which the banks have contracted by drafts, bills of exchange, bank and credit certificates, and bills payable at sight other than the bank notes issued. The composition of this reserve is the same as that of the reserve required for the security of the notes.

Banks of issue are forbidden to place new loans on real security. They may only conclude transactions which were entered upon before July 1, 1893. They are equally forbidden

¹ What is called in Italy, the *riscontrata*; see p. 12.

to open any accounts not secured by collaterals, either at the time of the opening of the account or subsequently. And with respect to investments, which we have seen amount to so great a sum, the law allows for their liquidation a period of ten years, at the rate of one-fifth for each biennial period. All liabilities covered by the surplus fund shall be considered as discharged.

In regard to the Banca d' Italia, if at the end of any biennial period, the liquidations have not reached the proportions required by law, the bank is required to assess on its stockholders, within the limits of the nominal capital (300,000,000 lire), such payments as are necessary for making the liquidation required; but this increase in the paid-up capital affords no basis for an increase of the bank's circulation. As regards the banks of Naples and of Sicily, the profits realized are to be employed in completing the sum total of demobilization (liquidation of the capital sunk in permanent investments) required for each biennial period. Any bank which does not, during any biennial period, complete the redemption of its investments to the extent required, and which does not, by means of new payments or dividends set apart for that purpose, cover the sum remaining to be redeemed, shall be deprived of the privilege of issuing notes, to a sum amounting to four times the uncovered balance, until the redemption required is properly effected. If, at the end of the second period of two years, the redemption of investments has taken place regularly as prescribed, the tax on circulation shall be reduced to one-fifth of the average rate of discount during the semester for which the tax is levied; but the tax must not in any case exceed one per cent. Banks doing business not countenanced by the law shall be subject to a tax equal to three times the rate of discount for all the illegal operations which have taken place, and for the entire period of time covered by the transactions.

At the expiration of each biennial period all new liabilities are to be charged as debits, while payments on liabilities are to

be entered as credits against the year during which they have been made, whether in whole or in part.

The banks of issue may receive deposits on account and pay interest on them, but in case the amount of these running accounts exceeds, for the Banca d' Italia, 130,000,000, for the Banca di Napoli 40,000,000, for the Banca di Sicilia 12,000,000 lire, the bank in question must reduce its circulation by an amount equal to three-fourths of the excess. The rate of interest allowed on running accounts bearing interest must not be more than one-half the rate of discount for the three years following the promulgation of the present law, and one-third of that rate for succeeding years.

The bank of issue may hold Italian bonds to an amount not exceeding, at current values, for the Banca d' Italia 70,000,000, for the Banca di Napoli 21,000,000, for the Banca di Sicilia 4,000,000. If they receive, in payment of debt or shares, securities or merchandise other than those permitted by law, such securities or merchandise are to be disposed of within a period of two years. They may also accept mortgages or good securities for unpaid debts, but these values must be disposed of within three years.

The banks of issue are permanently under the surveillance of the Minister of Agriculture, Industry, and Commerce, in conjunction with the Minister of the Treasury. Every two years, under the direction of these two ministers, there shall be had a special investigation of the banks of issue by officials who have not taken part in previous investigations of the bank which they are to investigate. The reports of these investigations shall be presented to Parliament within three months.

At the suggestion of the above named ministers, the power of issuing notes can be suspended or definitely withdrawn, by royal edict, from the bank which has violated the terms of the law governing banks of issue or of any particular statute. The directors of banks of issue are responsible, all and several, both to the stockholders, to the bank as a legal person, and to outsiders, for the proper execution of the bank law, and of the rules and regu-

lations of the bank, even apart from civil actions and penalties to which they may be liable by virtue of other laws. This solidarity of responsibility does not exist for the director who, not being implicated, has without delay recorded his dissension in the minutes of proceedings, and has given immediate notice of it in writing to the authorities.

Legal action may be taken against the directors by one or more of the stockholders, provided that the complainants possess at least 1,000 shares.

Members of Parliament can hold no office, paid or unpaid, in the banks of issue.

Article 20 of the law declares: "In case of transgressions of the dispositions of the present law, whoever, invested with any function in the banks of issue, shall misrepresent facts or conceal the truth, so as to mislead those whose duty it is to exercise the functions of surveillance or inspection, with a view to concealing from them any irregularity in the affairs of the bank, or any illegal transactions, or acts implicating a third party, shall be punished by imprisonment for not less than three months nor more than four years, together with temporary interdiction from the exercise of any public functions. * * * * Whosoever, in the exercise of the functions of surveillance or of inspection of the banks of issue, shall utter a false statement and conceal the truth, with the aims indicated by the preceding provisions, shall be punished by imprisonment for not less than one nor more than twenty years, with temporary interdiction from exercising any public function. * * * * Whosoever shall issue notes not printed and supplied to the banks in accordance with the provisions of Article 9, or shall reissue notes which should have been cancelled or destroyed, shall be punished by imprisonment for not less than three nor more than six years, with temporary interdiction from the exercise of any public function."

This article contains, so to speak, the philosophy of recent scandals, and aims at preventing the repetition of the frauds committed by the Banca Romana. But will it be effective?

Such are the principal dispositions of the law of the 10th of August last. This law has imposed a great many restrictions (perhaps too many) on the actions of banks of issue ; that it has provided, among other things, for the increase of the metallic reserve, for the gradual reduction of the circulation, and for the liquidation of immobilized capital. But while the law may decree the convertibility of our bank-notes, their convertibility is and will be none the less illusory, ineffective, and farcical for a long time to come. With the premium on gold at twelve per cent., and even when it is below that figure, the banks endeavor by all means to avoid redeeming their notes ; but the premium can not be wholly eliminated until the banks honor their engagements by redeeming their notes without evasion. It is, therefore, a vicious circle, and for the present there seems to be no way of escape from it.

Again, it is to be noted that the opposition between the banks still continues, for besides the Banca d'Italia, there are two other banks in operation, the Banca di Napoli and the Banca di Sicilia ; we shall still have new struggles between these three banks of issue, and we still lack a consistent management of the money market. However, there is ground to hope that the harsh experience of the past, the losses suffered, a consequent interest and more wide-awake vigilance, may preserve us from new errors in the management of banks of issue.

The financial situation of the State has been sensibly bettered ; the deficit remains, it is true, but it can be removed without much difficulty, for it has been greatly diminished, and it is, therefore, surely a great mistake to think that Italy is on the way to bankruptcy. The crisis is not due to the steady deficit, but to the scarcity of metallic money and the depreciation of bank notes. It will be relieved in proportion as the banks of issue retrieve the operations of the past and live up to the economic principles which their nature and their purpose require.

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